the group's consolidated taxable income determined without:

(1) Any depletion with respect to an oil or gas property (other than a gas property with respect to which the depletion allowance for all production is determined pursuant to section 613A(b)) for which percentage depletion would exceed cost depletion in the absence of the depletable quantity limitations contained in section 613A(c) (1) and (6) and the consolidated taxable income limitation contained in paragraph (a) of this section.

(2) Any consolidated net operating loss carryback to the consolidated return year under §§ 1.1502–21 or 1.1502-21A (as appropriate) and

(3) Any consolidated net capital loss carryback to the consolidated return year under § § 1.1502–22 or 1.1502-22A (as appropriate).

(c) *Allocation to oil and gas properties.* The maximum amount allowable as a deduction under section 613A(c), after the application of paragraph (a) of this section, is allocated to properties held by members in accordance with the regulations under section 613A(d). Those regulations provide for an initial allocation and possible reallocation of the maximum allowable percentage depletion deduction among oil and gas properties. Thus, if, after the initial allocation, cost depletion exceeds the percentage depletion that would be allowable for a particular oil or gas property, cost depletion must be used for that property and the maximum amount of percentage depletion allowable as a deduction for the group is reallocated among only the remaining properties held by all members.

(d) *Carryover for disallowed amounts.* (1) If any amount is disallowed as a deduction for the taxable year by reason of section 613A(d)(1) or paragraph (a) of this section, the disallowed amount for each oil or gas property is treated as an amount allowed as a deduction under section 613A(c), for the following taxable year for the member that owned the property, in accordance with the regulations under section 613A and paragraphs (a) and (d)(2) of this section.

(2) Any amount that was disallowed as a deduction in a separate return limitation year of a member may be carried to a consolidated return year only to the extent that 65 percent of the excess determined under paragraph (d)(3) of this section exceeds the sum of the otherwise allowable percentage depletion deductions for the member's oil and gas properties for the year.

(3) The excess determined in this subparagraph (3) for a member is the excess, if any, of adjusted consolidated taxable income for the year under paragraph (b) of this section over that income recomputed by excluding the items of income and deductions of the member.

(e) *Effective date.* This section applies to taxable years for which the due date (without extensions) for filing returns is after September 30, 1980.

[T.D. 7725, 45 FR 65561, Oct. 3, 1980, as amended by T.D. 8677, 61 FR 33324, June 27, 1996; T.D. 8823, 64 FR 36100, July 2, 1999]

§ 1.1502–47 Consolidated returns by life- nonlife groups.

(a) *Scope*—(1) *In general.* Under section 1504(b)(2), insurance companies that are taxed under section 802 or 821 (relating respectively to life insurance companies and to certain mutual insurance companies) are not treated as includible corporations for purposes of determining under section 1504(a) the existence of an affiliated group and the composition of its membership. Section 1504(c)(2) provides an election whereby certain life insurance companies and mutual insurance companies may be treated as includible corporations, and thus members, of a group composed of other includible corporations. This section provides regulations for the making of this election and for the determination of an electing group's composition and its consolidated tax liability.

(2) *General method of consolidation*—(i) *Subgroup method.* The regulations adopt a subgroup method to determine consolidated taxable income. One subgroup is the group's nonlife companies (including those taxable under section 821). The other subgroup is the group's life insurance companies. Initially, the nonlife subgroup computes nonlife consolidated taxable income and the life

subgroup computes consolidated partial life insurance company taxable income. A subgroup's income may in effect be reduced by a loss of the other subgroup. The life subgroup losses consist of consolidated loss from operations and life consolidated net capital loss. The nonlife subgroup losses consist of nonlife consolidated net operating loss and nonlife consolidated net capital loss. Consolidated taxable income is therefore defined in pertinent part as the sum of nonlife consolidated taxable income and consolidated partial life insurance company taxable income reduced by life subgroup losses or nonlife subgroup losses.

(ii) *Subgroup loss.* A subgroup loss does not actually affect the computation of nonlife consolidated taxable income or consolidated partial life insurance company taxable income. It merely constitutes a bottom-line adjustment in reaching consolidated taxable income. Furthermore, one subgroup's loss must first be carried back against income of the same subgroup before it may be used as a setoff against the second subgroup income in the taxable year the loss arose. (See section 1503(c)(1)). The carryback of the losses from one subgroup may not be used to offset income of the other subgroup in the year to which the loss is to be carried. This carryback of the first subgroup's loss may ''bump'' the second subgroup's loss that in effect previously reduced the income of the first subgroup. The second subgroup's loss that is bumped in appropriate cases may in effect reduce a succeeding year's income of the second or first subgroup. This approach gives the group the tax savings of the use of losses but the bumping rule assures that insofar as possible life deductions will be matched against life income and nonlife deductions against nonlife income.

(iii) *Carryover of subgroup loss.* A subgroup's loss may be used in a succeeding year, but in any particular succeeding year the loss must be used to reduce the income of the same subgroup before it may be used as a setoff against the other subgroup's income.

(3) *Authority.* This section is prescribed under the authority of sections 1502, 1503(c), 1504(c)(2), and 7805(b).

(4) *Other provisions.* The provisions of §§ 1.1502–1 through 1.1502–80 apply unless this section provides otherwise. Further, unless otherwise indicated in this section, a term used in this section has the same meaning as in sections 801–844.

(b) *Effective date.* This section is effective for taxable years for which the due date (without extensions) for filing returns is after March 14, 1983.

(c) *Cross references.* The following table provides cross references for some of the definitions and operating rules that are relevant in making the election and determining the group's composition and its tax liability:

Item and Paragraph
General definitions (d).
Eligible corporation (Five-year rules) (d)(12).
Election (e).
Consolidated taxable income (g).
Nonlife consolidated taxable income (h).
Consolidated partial life insurance company taxable income (j).
Nonlife subgroup losses (m).
Life subgroup losses (n).
Alternative tax (o).

(d) *Definitions.* For purposes of this section:

(1) *Life insurance company.* The term ''life company'' means a life insurance company as defined in section 801. Section 801 applies to each company separately.

(2) *Mutual insurance company.* The term ''mutual company'' means a mutual insurance company taxable under section 821(a)(1).

(3) *Life insurance company taxable income.* The term ''life insurance company taxable income'' is referred to as LICTI. The terms ''TII'', ''GO'', and ''LO'' refer, respectively, to taxable investment income (section 804), gain from operations (section 809), and loss from operations (section 812). The term ''consolidated partial LICTI'' refers to consolidated LICTI without section 802(b)(3).

(4) *Group.* The term ''group'' means an affiliated group of corporations (as defined in section 1504(a)). Unless otherwise indicated in this section, a group's composition is determined without section 1504(b)(2).

(5) *Member.* The term ''member'' means a corporation (including the

common parent) that is an includible corporation in the group. A life company or mutual company is tentatively treated as a member for any taxable year for purposes of determining if it is an eligible corporation under paragraph (d)(12) of this section and therefore if it is an includible corporation under section 1504(c)(2). If such a company is eligible and includible (under section 1504(c)(2)), it will actually be treated as a member of the group.

(6) *Life member.* A life member is a member of the group that is a life company.

(7) *Nonlife member.* A nonlife member is a member of the group that is not a life company.

(8) *Life subgroup.* A life subgroup is composed of those members that are life members. If the group has only one life member, it constitutes a life subgroup.

(9) *Nonlife subgroup.* A nonlife subgroup is composed of those members that are nonlife members. If the group has only one nonlife member, it constitutes a nonlife subgroup.

(10) *Separate return year.* The term ''separate return year'' means a taxable year of a corporation for which it files a separate return or for which it joins in the filing of a consolidated return by another group. For purposes of this subparagraph (10), the term ''group'' is defined with regard to section 1504(b)(2) for years in which an election under section 1504(c)(2) is not in effect. Thus, a separate return year includes a taxable year for which that election is not in effect.

(11) *Separate return limitation year.* Section 1.1502–1(f)(2) provides exceptions to the definition of the term ''separate return limitation year''. For purposes of applying those exceptions to this section, for taxable years ending after December 31, 1980, the term ''group'' is defined without regard to section 1504(b)(2) and the definition in this subparagraph (11) applies separately to the nonlife subgroup in determining nonlife consolidated taxable income under paragraph (h) of this section and to the life subgroup in determining consolidated partial LICTI under paragraph (j) of this section. Paragraph (m)(3)(ix) of this section defines the term ''separate return limitation year'' for purposes of determining whether the losses of one subgroup may be used against the income of the other subgroup.

(12) *Eligible corporations*—(i) *In general.* A corporation is an eligible corporation for a taxable year of a group only if, throughout every day of the base period the corporation:

(A) Was in existence and a member of the group determined without the exclusions in section 1504(b)(2) (see paragraphs (d)(12) (iii) through (vi) of this section),

(B) Was engaged in the active conduct of a trade or business (''active business''),

(C) Did not experience a change in tax character (see paragraph (d)(12)(vii) of this section), and

(D) Did not undergo disproportionate asset acquisitions (see paragraph (d)(12)(viii) of this section).

(ii) *Base period.* The base period consists of the common parent's five taxable years immediately preceding the group's taxable year for which the consolidated return and the determination of eligibility are made. Eligibility is determined for each consolidated return year beginning with the first year for which the election under section 1504(c)(2) is effective.

(iii) *In existence.* Except as provided in paragraphs (d)(12) (v) and (vi) of this section, a corporation organized after the base period begins is not eligible even though it is a member of the group immediately after its organization. For purposes of this subdivision (iii), a corporation that was a party to a reorganization described in section 368(a)(1)(F) shall be treated as the same entity both before and after the reorganization.

(iv) *Membership period.* Except as provided in paragraphs (d)(12) (v) and (vi) of this section, a corporation must have been a member of the group throughout the base period to be eligible. Thus, an ineligible corporation includes one whose stock was acquired from outside the group at any time during the base period or one which was a member of a different group (whether by application of reverse acquistion rules in §1.1502–75(d)(3) or otherwise) at any time during the base period. For purposes of this subdivision

(iv), the common parent of a group is treated as constituting a group (and hence is a member) during any period when it was not a member of an affiliated group within the meaning of section 1504(a) (applied without section 1504(b)(2)).

(v) *Tacking rule.* The period during which an ''old'' corporation is in existence and a member of the group engaged in active business is included in (or ''tacks'' onto) the period for the ''new'' corporation if the following five conditions listed in this subdivision (v) are met. For purposes of this subparagraph (12), a ''new'' corporation is a corporation (whether or not newly organized) during the period its eligibility depends upon the tacking rule. The five conditions are as follows:

(A) The first condition is that, at any time, 80 percent or more of the new corporation's assets it acquired (other than in the ordinary course of its trade or business) where acquired from the old corporation in one or more transactions described in section 351(a) or 381(a). This asset test is applied by using the fair market values of assets on the date they were acquired and without regard to liabilities. Assets acquired in the ordinary course of business will be excluded from total assets only if they were acquired after the new corporation became a member of the group (determined without section 1504(b)(2)). In addition, assets that the old corporation acquired from outside the group in transactions not conducted in the ordinary course of its trade or business are not included in the 80 percent (but are included in total assets) if the old corporation acquired those assets within five calendar years before the date of their transfer to the new corporation.

(B) The second condition is that at the end of the taxable year during which the first condition is first met, the old corporation and the new corporation must both have the same tax character. For purposes of this paragraph (d)(12), a corporation's tax character is the section under which it would be taxed (*i.e.*, sections 11, 802, 821, or 831) if it filed a separate return. If the old corporation is not in existence (or adopts a plan of complete liquidation) at the end of that taxable year, this subdivision (v)(B) will apply to the old corporation's taxable year immediately preceding the beginning of the taxable year during which the first condition is first met.

(C) The third condition is that, if the old and new corporation are life insurance companies, the transfer (or transfers) is not reasonably expected (at the time of the transfer) to result in the separation of profitable activities from loss activities.

(D) The fourth condition is that, at the end of the taxable year during which the first condition is first met, the new corporation does not undergo a disproportionate asset acquisition under paragraph (d)(12)(viii) of this section.

(E) The fifth condition is that, if there is more than one old corporation, the first three conditions apply to all of the corporations. Thus, the second condition (tax character) must be met by all of the old corporations transferring assets taken into account in meeting the test in paragraph (d)(12)(v)(A) of this section.

(vi) *Old group remaining in existence.* If the common parent of a group (or a new common parent) became the common parent in a transaction described in §1.1502–75 (d)(2) or (d)(3) where a group remained in existence, then paragraph (d)(12) (ii) through (iv) of this section apply by treating that common parent as if it were also the previous common parent of the group that remains in existence. If this paragraph (d)(12)(vi) applies to a transaction, the tacking rule in paragraph (d)(12)(v) of this section does not apply to the transaction.

(vii) *Change in tax character.* A corporation must not experience during the base period a change in tax character (as defined in paragraph (d)(12)(v)(B) of this section) if the change is attributable to an acquisition of assets from outside the group in transactions not conducted in the ordinary course of its trade or business. However, if a new corporation relies on the tacking rules in paragraph (d)(12)(v) of this section, this paragraph (d)(12)(vii) shall apply during the base period and the current consolidated return year and even if the change in tax

character is attributable to an asset acquisition from within the group.

(viii) *Disproportionate asset acquisition.* To be eligible, a corporation must not undergo during the base period disproportionate asset acquisitions which are attributable to an acquisition (or a series of acquisitions) of assets from outside the group in transactions not conducted in the ordinary course of its trade or business (special acquisition). Whether special acquisitions are disproportionate is determined at the end of each base period. Whether an acquisition results in a disproportionate asset acquisition depends on all of the facts and circumstances including the following factors and rules:

(A) One factor is the portion of the insurance reserves (*i.e.,* total reserves in section 801 (c)) of the acquiring company at the end of the base period which is attributable to special acquisitions.

(B) A second factor is the portion of the fair market value of the assets (without reduction for liabilities) of the acquiring company at the end of the base period that is attributable to special acquisitions.

(C) A third factor is the portion of the premiums generated during the last taxable year of the base period which are attributable to special acquisitions.

(D) A corporation will not experience a disproportionate asset acquisition unless 75 percent of one factor (whether or not listed in this subdivision (viii)) is attributable to special acquisitions.

(E) Money or other property contributed to a corporation by a shareholder that is not a member of the group (without section 1504(b)(2)) is not a special acquisition.

(F) If a new corporation relies on the tacking rules in paragraph (d)(12)(v) of this section, this subdivision (viii) applies to that corporation during a consolidated return year. Thus, if at any time during a consolidated return year, a new corporation undergoes a disproportionate asset acquisition, the corporation becomes ineligible at that time.

(13) *Ineligible corporation.* A corporation that is not an eligible corporation is ineligible. If a life company or mutual company is ineligible, it is not treated under section 1504(c)(2) as an includible corporation. Losses of a nonlife member arising in years when it is ineligible may not be used under section 1503(c)(2) and paragraph (m) of this section to set off the income of a life member. If a life or mutual company is ineligible and is the common parent of the group (without section 1504(b)(2)), the election under section 1504(c)(2) may not be made.

(14) *Illustrations.* The following examples illustrate this paragraph (d). In each example, L indicates a life company, another letter indicates a nonlife company, and each corporation uses the calendar year as its taxable year.

Example (1). P has owned all of the stock of S since 1913. On January 1, 1980, P purchased all of the stock of L_1 which owns all of the stock of L_2 and S_2. L_1 and L_2 are treated as members for purposes of determining if they are eligible for 1982. However, for 1982, L_1, L_2, and S_2 are ineligible because none of them has been a member of the group for P's five taxable years preceding 1982. For 1982, L_1 and L_2 may elect to file a consolidated return because they constitute an affiliated group under section 1504(c)(1), and P and S may file a consolidated return.

Example (2). Since 1974, P has been a mutual insurance company owning all the stock of L_1. In 1980, P transfers assets to S_1., a new stock casualty company subject to taxation under section 831(a). For 1982, only P and L_1 are eligible corporations. The tacking rule in paragraph (d)(12)(v) of this section does not apply in 1982 because the old corporation (P) and the new corporation (S_1) do not have the same tax character. The result would be the same if P were a life company.

Example (3). Since 1974, L has owned all the stock of L_1 which has owned all the stock of S_1, a stock casualty company. L_1 writes some accident and health insurance business. In 1980, L_1 transfers this business, and S_1 transfers some of its business, to a new stock casualty company, S_2., in a transaction described in section 351 (a). The property transferred to S_2. by L_1 had a fair market value of $50 million. The property transferred by S_1 had a fair market value of $40 million. S_2. is ineligible for 1982 because the tacking rule in paragraph (d)(12)(v) of this section does not apply. The old corporations (L_1 and S_1) and the new corporation (S_2.) do not all have the same tax character. See subparagraph (d)(12)(v)(B) and (E) of this section. The result would be the same if L_1 transferred other property (*e.g.,* stock and securities) with the same value, rather than accident and health insurance contracts, to S_2.

Example (4). Since 1974, P has owned all the stock of S and L_1. L_1 is a large life company

engaged in active business since 1974. On January 1, 1982, L_1 transfers in a section 351 (a) transaction assets (not acquired from outside the group) to a new life company, L_2. For 1982, L_2 is eligible because under paragraph (d)(12)(v) of this section, L_2 is considered to have been in existence and a member of the group engaged in the active business since 1974 which is the period L_1, the old corporation, was in existence and a member of the group so engaged.

Example (5). The facts are the same as in example (4). Assume that the fair market value of the assets L_1 transferred to L_2 was $10 million on January 1, 1982 and that L_2 acquired no other assets prior to June 30, 1983. Assume further that on January 1, 1983, L_1 acquires (other than in the ordinary course of its trade or business) assets having a fair market value of $40 million from L_3, an unrelated life company. On June 30, 1983, L_1 transfers those assets to L_2. L_2 becomes ineligible on June 30, 1983. Since by fair market values, 80 percent (*i.e.*, 40/50) of L_2's assets are attributable to special acquisitions, L_2 has undergone a disproportionate asset acquisition at that time. See paragraph (d)(12)(viii)(B), (D), and (F) of this section.

Example (6). The facts are the same as in example (5) except that L_1 transfers assets (other than life insurance contracts) having a fair market value of $40 million to L_2 and L_2 purchases the assets of L_3 on June 30, 1983. the result of the 1983 acquisition is the same as in example (5).

Example (7). The facts are the same as in example (5) except the acquired assets acquired by L_2 in 1983 from L_1 have a fair market value of $20 million. In 1983, L_2 had $1 million of premiums on its pre-existing contracts but premiums generated by the acquired business for the entire year would have been $2 million. L_2 is eligible in 1983 because it did not experience a disproportionate asset acquisition on June 30, 1983.

Example (8). Since 1974, L, a State A corporation, has owned all of the stock of L_1 and S_1. On January 1, 1982, L merges into L_3, a smaller State B corporation, which owns the stock of S_2. The transaction is a reverse acquisition described in §1.1502–75(d)(3) and the group of which L was the common parent remains in existence. Under paragraph (d)(12)(vi) of this section, L_3 is eligible for 1982. However, S_2 is ineligible in 1982 under paragraph (d)(12)(iv) of this section.

Example (9). The facts are the same as in example (8) except that L acquires the stock of L_3. L_3 and S_2 are both ineligible for 1982. On January 1, 1983, the fair market value of L_3's assets are $5 million (without liabilities) and on that date L transfers assets (not acquired from outside the group) having a fair market value of $95 million (without liabilities) to L_3. L and L_3 are life companies at the end of 1983. L_3 is eligible in 1983 under the tacking rule in paragraph (d)(12)(v) of this section. S_2 is ineligible in that year. The result would be the same if L_3 was not a life company prior to January 1, 1983. See paragraph (d)(12)(v)(B) of this section.

Example (10). Since 1974, P has owned all of the stock of S_1 and L_1. On January 1, 1982, L_1 incorporates L_2 and transfers cash and securities to L_2. L_2 begins writing a new line of specialty life insurance products and it qualifies as a life company for calendar year 1982. L_2 generates a loss from operations (section 812) attributable to its writing of new business. For 1982, L_2 is ineligible under paragraph (d)(12)(v)(C) of this section.

Example (11). The facts are the same as in example (10) except that L_1 transfers to L_2 a block of insurance contracts that generated losses for L_1 and continued to generate losses for L_2, producing a loss from operations. L_2 is ineligible in 1982 under paragraph (d)(12)(v)(C) of this section.

Example (12). Since 1974, X, a foreign corporation, has owned all the stock of S_2 and S_1, and S_1 has owned all of the stock of L_1. On January 1, 1982, X incorporates a new U.S. company P, and transfers the stock of S_1 and S_2 to P. Assume that under §1.1502–75(d)(3) (relating to reverse acquisitions), the S_1–L_1 affiliated group remains in existence. Under paragraph (d)(12)(vi) of this section, P, S_1, and L_1 are eligible but S_2 is ineligible. The result would be the same if X were an individual.

Example (13). The facts are the same as in example (12) except that X owns all of the stock of S_1, L_1, and S_2. In addition, on January 1, 1982, X transfers the stock of S_1 and S_2 to L_1. L_1 is eligible in 1982 under paragraph (d)(12)(iv) of this section. L_1 would still be eligible even if it owned a subsidiary during the base period but sold the subsidiary prior to January 1, 1982. S_1 and S_2 are ineligible in 1982.

Example (14). Since 1974, S_1 has owned all of the stock of L_1. S_2, an unrelated company, has owned all of the stock of L_2 and S_3 for 10 years. S_1 and S_2 are active stock casualty companies and not holding companies. On January 1, 1982, S_1 and S_2 merge into a new casualty company, S, in a transaction described in §1.1502–75(d)(3) so that the group of which S_1 was the common parent remains in existence. S and L_1 are eligible in 1982 under paragraph (d)(12)(vi) of this section. L_2 and S_3 are ineligible.

Example (15). The facts are the same as in example (14) except that S_2 (the first corporation in §1.1502–75(d)(3)) acquires the stock of S_1 in exchange for the stock of S_2. The result is that only S_2, S_1, and L_1 are eligible in 1982.

Example (16). Since 1974, S had owned all of the stock of L_1. L_1 is a large life company. On January 1, 1982, L_1 incorporates L_2 and transfers $40 million in cash and securities to L_2 in a transaction described in section

351(a). On March 1, 1982, L_2 purchases the assets of L_3, an unrelated life company. The purchased assets have a fair market value (without liabilities) of $30 million on March 1, 1982. L_2 is ineligible for 1982 because the tacking rule in paragraph (d)(12)(v) of this section does not apply. L_2 experienced a disproportionate asset acquisition in 1982. See paragraph (d)(12)((v)(D) of this section.

(e) *Election*—(1) *In general.* The election under section 1504(c)(2) may not be made if the group's common parent is an ineligible life company or an ineligible mutual company. The election under section 1504(c)(2) may only be made by the common parent of the group (as defined in section 1504(c)(2) without the exclusions in section 1504(b)(2)). For example, assume that P owns all of the stock of L_1, an eligible life company, which owns the stock of S_1. Assume further that P also owns the stock of L_2, an ineligible life member, which (for more than five years) has owned the stock of a nonlife company, S_2. Only P may make the election and, if it does so, P, L_1, and S_1 may file a consolidated return under this section. L_2 may not make the election under section 1504(c)(2) and may not file a consolidated return with S_2.

(2) *How election is made*—(i) *General rule.* The election under section 1504(c)(2) is generally made by the group's common parent in the same manner (and it has the same effect) as the election to file a consolidated return is made under §1.1502–75 (a) and (b) for a group which did not file a consolidated return for the immediately preceding taxable year. The procedure for making the election under section 1504(c)(2) is the same whether or not a consolidated return was filed by the life members or the nonlife members for the immediately preceding taxable year.

(ii) *Special rule.* Notwithstanding the general rule, however, if the nonlife members in the group filed a consolidated return for the immediately preceding taxable year and had executed and filed a Form 1122 that is effective for the preceding year, then such members will be treated as if they filed a Form 1122 when they join in the filing of a consolidated return under section 1504(c)(2) and they will be deemed to consent to the regulations under this section. However, an affiliation schedule (Form 851) must be filed by the group and the life members must execute a Form 1122 in the manner prescribed in §1.1502–75(h)(2).

(3) *Irrevocability.* Except as provided in §1.1502–75(c) and paragraph (e)(4) of this section, the election under section 1504(c)(2) is irrevocable.

(4) *Permission to discontinue*—(i) *General rule.* A ''section 1504(c)(2) group'' with a common parent that has made the election to file a consolidated return under section 1504(c)(2) in a previous taxable year is granted permission to elect (under §1.1502–75(c)(2)(ii)) to discontinue filing such a consolidated return for that group's first taxable year for which the regulations under this section are effective. This election to discontinue shall be exercised in the time and manner prescribed in §1.1502–75(c)(3), except that the group's common parent shall exercise this election to discontinue (and the other members of the section 1504(c)(2) group must comply with this election) by filing appropriate returns. For purposes of this paragraph (e)(4), an appropriate return is either a separate return or a consolidated return that is filed by newly exercising the privilege under §1.1502–75(a)(1).

(ii) *Types of groups.* (A) A ''section 1504(c)(2) group'' is an affiliated group which files or filed a consolidated return pursuant to an election under section 1504(c)(2).

(B) A ''limited group'' is an affiliated group (determined without section 1504(c)(2)) having at least one member which was a member of a section 1504(c)(2) group on the date that the section 1504(c)(2) group elected to discontinue under paragraph (e)(4)(i) of this section.

(iii) *Effect on restoration rules.* If a group ceases to file a consolidated return or terminates or if a member leaves the group, certain items of income, gain, or loss on transactions between members are taken into account under §§1.1502–13, 1.1502–18, and 1.1502–19 (''restoration rules''). For purposes of applying these restoration rules solely by reason of an election under paragraph (e)(4)(i) or (e)(4)(v)(A) of this section to discontinue filing consolidated returns as a section 1504(c)(2) group, the following rules apply:

(A) The section 1504(c)(2) group shall not be considered to terminate and no member of that group shall be treated as ceasing to be a member.

(B) Members of that section 1504(c)(2) group that are included in the consolidated return of a limited group for the first taxable year for which the discontinuance is effective shall be considered to be filing a consolidated return as a continuation of the section 1504(c)(2) group. However, a corporation that is not a member of a particular limited group for that taxable year is considered to have a separate return year (and, for purposes of §1.1502–19(c), not to be a member of a group filing a consolidated return) with respect to that limited group's members.

(C) Section 1.1502–13 shall be applied without regard to paragraph (f)(1)(vii).

(iv) *Illustrations.* The following examples illustrate paragraph (e)(4)(i)–(iii) of this section. In these examples, L indicates a life company and another letter indicates a nonlife company. All corporations use the calendar year as the taxable year. For all taxable years involved, P owns all the stock of L_1 and of S, L_1 owns all the stock of L_2, L_2 owns all the stock of L_3, and S owns all the stock of L_4. For 1981, P makes the life-nonlife election of section 1504(c)(2) and L_4 is an eligible corporation. For 1982, P makes the election to discontinue filing consolidated returns under section 1504(c)(2) in accordance with the permission granted in this paragraph (e)(4).

Example (1). L_1, L_2, and L_3 were eligible members. For 1982, P and S may either file separate returns or may file, as a limited group, a consolidated return. Similarly, L_1, L_2, and L_3 may either file separate returns or may file a consolidated return as a limited group under section 1504(c)(1). L_4 must file a separate return.

Example (2). For 1981, L_1 was an ineligible member and L_1, L_2, and L_3 filed a consolidated return under section 1504(c)(1). For 1982, L_1, L_2, and L_3 must continue filing a consolidated return under section 1504(c)(1).

Example (3). For 1981, L_1 was an eligible member and L_2 and L_3 were ineligible members. For 1982, L_1, L_2, and L_3 either must each file a separate return or must file a consolidated return as a limited group under section 1504(c)(1) having L_1 as a common parent.

Example (4). The facts are the same as in example (3). Assume further that for 1981, L_2 and L_3 file a consolidated return. During 1981, intercompany transactions (see §1.1502–13) occur in the life-nonlife group between P and L_1, between P and S, and between S and L_4 and occur in the ineligible life subgroup between L_2 and L_3. For 1982, the restoration rules of §1.1502–13, as modified by paragraph (e)(4)(iii)(B) of this section, will be applicable as indicated in the following table:

Intercompany transactions between	§1.1502–13
P and L_1	Yes.
P and S, if they file:	
Separate returns	Yes.
A consolidated return	No.
S and L_4	Yes.
L_2 and L_3, if L_1, L_2, and L_3 file:	
Separate returns	Yes.
A consolidated return	No.

(v) *Additional rules.* (A) If a group with a taxable year ending in the month of December, 1982, had made the election under section 1504(c)(2) for a taxable year ending prior to December 1, 1982, and if that group meets the conditions of subdivision (vi) of this paragraph (e)(4), then the common parent may elect to discontinue filing a consolidated return for its taxable year ending in the month of December, 1982 (and other members of the section 1504(c)(2) group must comply with this election) by filing appropriate returns (see paragraph (e)(4)(i) of this section) before September 16, 1983.

(B) If a group made the election under section 1504(c)(2) for its taxable year ending in the month of December, 1982, and if that group meets the conditions of subdivision (vi) of this paragraph (e)(4), then the common parent may elect to withdraw the section 1504(c)(2) election (and all other members of the group determined without section 1504(b)(2) comply with the election) by filing before September 16, 1983, any returns for the appropriate taxable years that would have been filed had the section 1504(c)(2) election never been made.

(vi) A group referred to at subdivision (v)(A) or (B) of this (e)(4) meets the conditions of this subdivision (vi) if it—

(A) filed before March 16, 1983, a return for its taxable year ending in the month of December, 1982, and

(B) had not been granted an extension of time beyond March 15, 1983, for the filing of that return.

(vii) *Interest.* For purposes of section 6601(a), interest runs from the original due date (without extensions) for the filing of such returns as are filed pursuant to an election (to discontinue or withdraw as the case may be) under this paragraph (e)(4).

(5) *Consent to regulations.* If a group does not discontinue filing a consolidated return under paragraph (e)(4) of this section but continues to file a consolidated return for the group's first taxable year for which the regulations under this section are first effective, the members of the group will be deemed to have consented to the regulations under this section.

(6) *Cross reference.* If an election is made under section 1504(c)(2), see §1.1502–75 (e) and (f) for rules that apply for not including (or including) a member or a nonmember in the consolidated return.

(f) *Effect of election.* If the common parent makes the election under section 1504(c)(2), the following rules apply:

(1) *Termination of group.* A mere election under section 1504(c)(2) will not cause the creation of a new group or the termination of an affiliated group that files a consolidated return in the immediately preceding taxable year.

(2) *Effect of eligibility.* If a life member is eligible after an election under section 1504(c)(2), it may not be included as a member of an affiliated group as defined in section 1504(c)(1).

(3) *Eligible and ineligible life companies.* If any life company was a member of an affiliated group of life companies (as defined in section 1504(c)(1)) but is ineligible for a taxable year for which the election under section 1504(c)(2) is effective, that year is not a separate return year merely by reason of the election under section 1504(c)(2) in applying §§1.1502–13, 1.1502–18, and 1.1502–19 to transactions occurring in prior consolidated return years of that affiliated group. In addition, if more than one ineligible life member of the group (as defined in section 1504(c)(1)) joined in the filing of a consolidated return in the taxable year immediately preceding the year for which the election under section 1504(c)(2) is effective and, solely as a result of the election, one of the ineligible life members becomes the common parent of such a group (section 1504(c)(1)), the group must continue to file a consolidated return. For example, assume that L_1 owns all of the stock of S_1 and all of the stock of L_2. L_2 owns the stock of L_3. L_1, L_2, and L_3 are life companies and S_1 is a nonlife company. Assume further that in 1981, L_1, L_2, and L_3 file a consolidated return but L_1 makes the election under section 1504(c)(2) for 1982 and L_2 and L_3 are ineligible. L_2 and L_3 must continue to file a consolidated return in 1982. Moreover, L_2 could elect in 1982 to file a consolidated return (section 1504(c)(1)) with L_3 even if they did not file a consolidated return in 1981 with L_1.

(4) *Inclusion of life company.* If a life company is ineligible in the consolidated return year for which the election is effective, it will be treated as an includible corporation for the common parent's first taxable year in which the company becomes eligible.

(5) *Dividends received deduction.* Section 243(b)(5) defines the term affiliated group for purposes of the election to deduct 100 percent of the qualifying dividends received by a member from another member of the group. Section 246(b)(6) limits certain multiple tax benefits and the deduction itself. Section 243(b) (5) and (6) do not apply to the mutual companies and life companies that are eligible corporations. See section 1504(c)(2)(B)(i). Thus, the common parent of the group may elect to deduct 100 percent of the qualifying dividends received from an ineligible life company.

(6) *Controlled group.* Sections 1563 (a)(4), (b)(2)(D), and (b)(3)(C) (insofar as it applies to corporations described in section 1563(b)(2)(D)) do not apply to any eligible or ineligible life company that is a member of the group for a taxable year during which the election is effective. See paragraph (d)(4) of this section for the definition of group.

(7) *Consolidated tax.* The tax liability of a group for a consolidated return year (before application of credits against that tax) is computed on a consolidated basis by adding together the following taxes:

(i) The tax imposed under section 11 on consolidated taxable income (as determined under paragraph (g) of this

section). The taxes imposed under sections 802(a), 821(a), and 831(a) will each be treated as a tax imposed under section 11.

(ii) The tax imposed by section 1201 on consolidated net capital gain (as determined under paragraph (o) of this section) in lieu of the tax imposed under paragraph (f)(7)(i) of this section on that gain.

(iii) Any taxes described in §1.1502–2 (other than by paragraphs (a), (f), and (h) thereof).

(g) *Consolidated taxable income.* The consolidated taxable income is the sum of the following three amounts:

(1) *Nonlife consolidated taxable income.* The nonlife consolidated taxable income (as defined in paragraph (h) of this section) of the nonlife subgroup, as set off by the life subgroup losses as provided in paragraph (n) of this section. The amount in this paragraph (g)(1) may not be less than zero.

(2) *Consolidated partial LICTI.* The consolidated partial LICTI (as defined in paragraph (j) of this section) of the life subgroup, as set off by the nonlife subgroup losses as provided in paragraph (m) of this section. The amount in this paragraph (g)(2) may not be less than zero.

(3) *Surplus accounts.* The sum of the amounts subtracted under section 815 from the policyholders' surplus accounts of the life members.

(h) *Nonlife consolidated taxable income*—(1) *In general.* Nonlife consolidated taxable income is the consolidated taxable income of the nonlife subgroup, computed under §1.1502–11 as modified by this paragraph (h). For this purpose, separate taxable income of a member includes separate mutual insurance company taxable income (as defined in section 821(b)) and insurance company taxable income (as defined in section 832).

(2) *Nonlife consolidated net operating loss deduction*—(i) *In general.* In applying §§1.1502–21 or 1.1502-21A (as appropriate), the rules in this subparagraph (2) apply in determining for the nonlife subgroup the nonlife net operating loss and the portion of the nonlife net operating loss carryovers and carrybacks to the taxable year.

(ii) *Nonlife CNOL.* The nonlife consolidated net operating loss is determined under §§1.1502–21(A)(f) or 1.1502-21(e) (as appropriate) by treating the nonlife subgroup as the group.

(iii) *Carryback.* The nonlife consolidated net operating loss for the nonlife subgroup is carried back under §§1.1502–21A or 1.1502-21 (as appropriate) to the appropriate years (whether consolidated or separate) before the loss may be used as a nonlife subgroup loss under paragraphs (g)(2) and (m) of this section to set off consolidated partial LICTI in the year the loss arose. The election under section 172(b)(3)(C) to relinquish the entire carryback period for the net operating loss of the nonlife subgroup may be made by the common parent of the group. Furthermore, the election may be made even though the election under section 812(b)(3) and paragraph (l)(3)(iii) of this section is not made.

(iv) *Subgroup rule.* In determining the portion of the nonlife consolidated net operating loss that is absorbed when the loss is carried back to a consolidated return year beginning after December 31, 1981, §§1.1502–21A or 1.1502-21 (as appropriate) is applied by treating the nonlife subgroup as the group. Therefore, the absorption is determined without taking into account any life subgroup losses that were previously reported on a consolidated return as setting off nonlife consolidated taxable income for the year to which the nonlife loss is carried back.

(v) *Carryover.* The portion of the nonlife consolidated net operating loss that is not absorbed in a prior year as a carryback, or as a nonlife subgroup loss that set off consolidated partial LICTI for the year the loss arose, constitutes a nonlife carryover under this subparagraph (2) to reduce nonlife consolidated taxable income before that portion may constitute a nonlife subgroup loss that sets off consolidated partial LICTI for a particular year.

(vi) *Transitional rules.* The nonlife consolidated net operating loss deduction is subject to a transitional rule limitation in paragraph (h)(3) of this section.

(vii) *Example.* The following example illustrates this paragraph (h)(2). In the example, L indicates a life company,

another letter indicates a nonlife company, and each corporation uses the calendar year as its taxable year.

Example. P owns all of the stock of S and L_1. L_1 owns all of the stock of L_2. For 1982, the group first files a consolidated return for which the election under section 1504(c)(2) is effective. P and S filed consolidated returns for 1979 through 1981. In 1982, the P–S group sustains a nonlife consolidated net operating loss. The loss is carried back to the consolidated return years 1979, 1980, and 1981 of P and S by using the principles of §§1.1502–21A and 1.1502–79A and, because the election in 1982 under section 1504(c)(2) does not result under paragraph (f)(1) of this section in the creation of a new group or the termination of the P–S nonlife group, the loss is absorbed on the consolidated return in those years without regard to whether the loss in 1982 is attributable to P or S and without regard to their contribution to consolidated taxable income in 1979, 1980, or 1981. The portion of the loss not absorbed in 1979, 1980, and 1981 may serve as a nonlife subgroup loss in 1982 that may set off the consolidated partial LICTI of L_1 and L_2 under paragraphs (g)(2) and (m) of this section.

(3) *Transitional rule*—(i) *In general.* The portion of the nonlife consolidated net operating loss deduction in a consolidated return year beginning after December 31, 1980 (referred to as ''post-1980 year'') attributable to net operating losses sustained in separate return years ending before January 1, 1981 (referred to as ''pre-1981 year''), is subject to the rules and limitations in this subparagraph (3).

(ii) *Separate nonlife groups.* To determine the limitation, first, identify for the post-1980 year one or more separate affiliated groups of nonlife companies (as defined in section 1504 without section 1504(c)(2)). For this purpose, a single nonlife company may constitute a separate affiliated group if (A) it is not otherwise a member of a separate group or (B) it has a net operating loss sustained in the pre-1981 year that may be carried over and that year is a separate return limitation year (determined under §1.1502–1(f) without paragraph (d)(11) of this section).

(iii) *Carryover.* Second, identify the pre-1981 year net operating losses that may be carried over and that are attributable to each separate affiliated group of nonlife companies. The separate return limitation year rules in §§1.1502–21A(c) or 1.1502-21(c) (as appropriate) do not apply to any of these carryovers.

(iv) *Limitation.* Third, treat the last taxable year ending before January 1, 1981, as if in that year there was a consolidated return change of ownership of each such separate affiliated group of nonlife companies and apply the consolidated return change of ownership limitation in §1.1502–21A(d) to the losses of each group by treating the members of each separate group as old members.

(v) *Examples.* The following examples illustrate this paragraph (h)(3). In the examples L indicates a life company, another letter indicates a nonlife company, and each corporation uses the calendar year as its taxable year.

Example (1). Throughout all of 1982, P owns all of the stock of S and L_1 and L_1 owns all of the stock of L_2 which in turn owns all of the stock of S_1. Thus, for 1982, there are two nonlife subgroups under this subparagraph (3), P–S and S_1. For 1981, P and S did not file a consolidated return and for 1980 P has a net operating loss of $200,000. Assume that P had no income in 1981. For 1982, the group makes an election under section 1504(c)(2) to file a consolidated return and all corporations are eligible corporations. The consolidated taxable income for the nonlife subgroup for 1982 (determined without the consolidated net operating loss deduction) recomputed by including only items of income and deduction of P and S is $120,000. If $120,000 is the §1.1502–21(d)(2) amount for P and S, then the amount of P's net operating loss for 1980 that may be carried over to P and S for 1982 cannot exceed $120,000.

Example (2). (a) P owns all of the stock of S_1. On January 1, 1979, P purchased all of the stock of L_1 which owns all of the stock of L_2 and S_2. Prior to 1984, all of the corporations filed separate returns. For 1984, the group makes an election under section 1504(c)(2) to file a consolidated return.

(b) 1981, 1982, and 1983 are not treated under paragraph (d)(11) of this section as separate return limitation years of the P, S_1, and S_2 nonlife subgroup. However, P and S_1 will be treated as old members under paragraph (h)(3)(iv) of this section and under §1.1502–21A(d) with respect to their losses in 1979 and 1980 (whether a consolidated return was filed or separate returns were filed) so that the portion of nonlife consolidated taxable income attributable to S_2 may not absorb the losses of P or S_1. The rules that apply to the P–S_1 nonlife subgroup for 1979 and 1980 apply in an identical way to S_2 by treating S_2 as a subgroup separate from the P–S_1 nonlife subgroup. See section 1507(c)(2)(A) of the Tax Reform Act of 1976.

(c) Similarly, L_1 and L_2 are treated as old members under paragraphs (l)(3) and (h)(3)(iv) of this section for losses arising in 1979 and 1980. However, since the L_1—L_2 subgroup is also the life subgroup under paragraph (d)(8) of this section, the limitation in paragraph (h)(3)(iv) of this section does not affect the computation of consolidated partial LICTI for the life subgroup.

(4) *Nonlife consolidated capital gain net income or loss*—(i) *In general.* In applying §§1.1502–22 or 1.1502-22A (as appropriate),the rules in this subparagraph (4) apply in determining for the nonlife subgroup the nonlife consolidated capital gain net income or loss and the portion of the nonlife net capital loss carryovers and carrybacks to the taxable year. In particular, the nonlife consolidated capital gain net income and nonlife consolidated net capital loss are determined under the principles of §§1.1502–22 or 1.1502-22A(a) (as appropriate) by treating the nonlife subgroup as the group.

(ii) *Additional principles.* In applying §§1.1502–22A or 1.1502-22 to nonlife consolidated net capital loss carryovers and carrybacks, the principles set forth in paragraphs (h)(2) (iii) through (v) for applying §§1.1502–21 or 1.1502-21A (as appropriate) to nonlife consolidated net operating loss carryovers and carrybacks shall also apply. Further, the portion of nonlife consolidated net capital loss carryovers attributable to losses sustained in taxable years ending before January 1, 1981, is subject to the limitations in paragraph (h)(3) of this section applied by substituting ''net capital loss'' for the term ''net operating loss'' and ''§1.1502–22A(d)'' for ''§1.1502–21A(d)''.

(iii) *Special rules.* The nonlife consolidated net capital loss is reduced, for purposes of determining the carryovers and carrybacks under §§1.1502–22A(b)(1) or 1.1502-22(b) by the lesser of:

(A) The aggregate of the additional capital loss deductions allowed under section 822(c)(6) or section 832(c)(5), or

(B) The nonlife consolidated taxable income computed without capital gains and losses.

(i) [Reserved]

(j) *Consolidated partial LICTI.* [Reserved]

(k) *Consolidated TII*—(1) *General rule.* [Reserved]

(2) *Separate TII.* [Reserved]

(3) *Company's share of investment yield.* [Reserved]

(4) *Life consolidated capital gain net income.* [Reserved]

(5) *Life consolidated net capital loss carryovers and carrybacks.* The life consolidated net capital loss carryovers and carrybacks for the life subgroup are determined by applying the principles of §§1.1502–22 or 1.1502–22A (as appropriate) as modified by the following rules in this subparagraph (5):

(i) Life consolidated net capital loss is first carried back (or apportioned to the life members for separate return years) to be absorbed by life consolidated capital gain net income without regard to any nonlife subgroup capital losses and before the life consolidated net capital loss may serve as a life subgroup capital loss that sets off nonlife consolidated capital gain net income in the year the life consolidated net capital loss arose.

(ii) If a life consolidated net capital loss is not carried back or is not a life subgroup loss that sets off nonlife consolidated capital gain net income in the year the life consolidated net capital loss arose, then it is carried over to the particular year under this paragraph (k)(5) first against life consolidated capital gain net income before it may serve as a life subgroup capital loss that sets off nonlife consolidated capital gain net income in that particular year.

(iii) *Section 818(f).* Capital losses may not be deducted more than once and capital gain will not be included more than once. See section 818(e) and also section 818(f).

(iv) Capital loss carryovers are subject to the transitional rule in paragraph (k)(6) of this section.

(6) *Transitional rule.* The portion of the life consolidated capital loss carryovers attributable to the net capital losses of the life members sustained in separate return years ending before January 1, 1981, is subject to the same limitations as the capital losses of nonlife members in paragraph (h)(4)(iii) of this section by applying the principles of paragraph (h)(3) of this section to each separate affiliated group of life companies.

(l) *Consolidated GO or LO*—(1) *General rule.* [Reserved]

(2) *Separate GO.* [Reserved]

(3) *Consolidated operations loss deduction*—(i) *General rule.* The consolidated operations loss deduction is an amount equal to the consolidated operations loss carryovers and carrybacks to the taxable year. The provisions of §§1.1502–21 or 1.1502–21A (as appropriate) and section 812 apply to the extent not inconsistent with this paragraph (l)(3).

(ii) *Consolidated offset.* For purposes of applying section 812 (b) and (d), the term ''consolidated offset'' means the increase in the consolidated operations loss deduction which reduces consolidated partial LICTI to zero. For setoff of consolidated LO against nonlife consolidated taxable income, see paragraph (n)(2) of this section.

(iii) *Carrybacks.* A consolidated LO is first carried back to be absorbed by GO of a life member under section 809(d)(4) or consolidated partial LICTI (as the case may be under section 818(f)(2)) for prior consolidated return years (or apportioned to the life members for prior separate return years) without regard to any nonlife subgroup losses that were set off against consolidated partial LICTI and before the consolidated LO may serve as a life subgroup loss to be set off against nonlife consolidated taxable income in the year the consolidated LO arose. The election to relinquish the entire carryback period for the consolidated LO of the life subgroup may be made by the common parent of the group. See section 812(b)(3). Furthermore, the election may be made even though the election under section 172(b)(3)(C) and paragraph (h)(2)(iii) of this section is not made.

(iv) *Carryovers.* If a consolidated LO is not carried back or is not applied as a life subgroup loss that set off nonlife consolidated taxable income in the year the consolidated LO arose, then it is carried over to a particular year under this paragraph (l)(3) first against the GO of a life member under section 809(d)(4) or consolidated partial LICTI (as the case may be under section 818(f)(2)) before it may serve as a life subgroup loss that may be set off against nonlife consolidated taxable income for that particular year.

(v) *Transitional rule.* The portion of a consolidated operations loss deduction that is attributable to LOs sustained in separate return years ending before January 1, 1981, is subject to the same rules and limitations that the nonlife consolidated net operating loss deduction is subject to in paragraph (h)(3) of this section as applied by identifying separate affiliated groups of life companies.

(4) *Life consolidated capital gain net income or loss.* Life consolidated capital gain net income or loss is determined in the same manner as under paragraph (k)(4) of this section. However, a life member's company share is determined under section 809 (a) and (b)(3).

(m) *Consolidated partial LICTI setoff by nonlife subgroup losses*—(1) *In general.* The nonlife subgroup losses consist of the nonlife consolidated net operating loss and the nonlife consolidated net capital loss. Under paragraph (g)(2) of this section, consolidated partial LICTI is set off by the amounts of these two consolidated losses specified in paragraph (m)(2) of this section. The setoff is subject to the rules and limitations in paragraph (m)(3) of this section.

(2) *Amount of setoff*—(i) *Current year.* Consolidated partial LICTI for the current taxable year is set off by the portion of the nonlife consolidated net operating loss and nonlife consolidated net capital loss arising in that year that cannot be carried back under paragraph (h) of this section to prior taxable years (whether consolidated or separate return years) of the nonlife subgroup.

(ii) *Carryovers.* The portion of the offsettable nonlife consolidated net operating loss or nonlife consolidated net capital loss that has not been used as a nonlife subgroup loss setoff against consolidated partial LICTI in the year it arose may be carried over to succeeding taxable years under the principles of §§1.1502–21 or 1.1502–21A (as appropriate) (relating to net operating loss deduction) or §§1.1502–22 or 1.1502–22A (as appropriate) (relating to net capital loss carryovers). However, in any particular succeeding year, the losses will be used under paragraph (h) of this section in computing nonlife consolidated taxable income before being used in that year as a nonlife

subgroup loss that sets off consolidated partial LICTI.

(3) *Nonlife subgroup loss rules and limitations.* The nonlife subgroup losses are subject to the following operating rules and limitations:

(i) *Separate return years.* The carryovers in paragraph (m)(2)(ii) of this section may include net operating losses and net capital losses of the nonlife members arising in separate return years ending after December 31, 1980, that may be carried over to a succeeding year under the principles (including limitations) of §§1.1502–21 and 1.1502–22 (or §§1.1502–21A and 1.1502–22A, as appropriate). But see subdivision (ix) of this paragraph (m)(3).

(ii) *Capital loss.* Nonlife consolidated net capital loss sets off consolidated partial LICTI only to the extent of life consolidated capital gain net income (as determined under paragraph (l)(4) of this section) and this setoff applies before any nonlife consolidated net operating loss sets off consolidated partial LICTI.

(iii) *Capital gain.* Life consolidated capital gain net income is zero in any taxable year in which the life subgroup has a consolidated LO and, in any taxable year, it may not exceed consolidated partial LICTI.

(iv) *Ordering rule.* Consolidated partial LICTI for a consolidated return year is set off by nonlife subgroup losses for that year before being set off (under paragraph (m)(2)(ii) of this section) by a carryover of a nonlife subgroup loss to that year.

(v) *Setoff at bottom line.* The setoff of nonlife subgroup losses against consolidated partial LICTI does not affect life member deductions that depend in whole or in part on GO or TII. Thus, the setoff does not affect the amount of consolidated partial LICTI (as determined under paragraph (j) of this section) for any taxable year but it merely constitutes an adjustment in arriving at the group's consolidated taxable income under paragraph (g) of this section.

(vi) *Ineligible nonlife member.* (A) The offsetable nonlife consolidated net operating loss that arises in any consolidated return year (that may be set off against consolidated partial LICTI in the current taxable year or in a succeeding taxable year) is the amount computed under paragraph (h)(2)(ii) of this section reduced by the ineligible NOL. For purposes of this subparagraph (3), the ''ineligible NOL'' is in the year the loss arose the amount of the separate net operating loss (determined under §§1.1502–21(b) of any nonlife member that is ineligible in that year (and not the portion of the nonlife consolidated net operating loss attributable under §§1.1502–21(b) to such a member). (B) The carryovers of offsetable nonlife net operating losses under paragraph (m)(2)(ii) of this section do not include an ineligible NOL arising in a consolidated return year or a loss attributable to an ineligible member arising in a separate return year. See section 1503(c)(2). (C) For absorption within the nonlife subgroup of an ineligible NOL arising in a consolidated return year or a loss of an ineligible member arising in a separate return year which is not a separate return limitation year under paragraph (m)(3)(ix) of this section, see paragraph (m)(3)(vii) of this section.

(vii) *Absorption of ineligible NOL.* (A) If all or a portion of a nonlife member's ineligible NOL (determined under paragraph (m)(3)(vi)(A) of this section) may be carried back or carried over under paragraph (h)(2) of this section to a particular consolidated return year of the nonlife subgroup (absorption year), then notwithstanding §1.1502–21A(b)(3)(ii) or 1.1502–21(b), the amount carried to the absorption year will be absorbed by that member's contribution (to the extent thereof) to nonlife consolidated taxable income for that year.

(B) For purposes of (A) of this subdivision (vii), a member's contribution to nonlife consolidated taxable income for an absorption year is the amount of such income (computed without the portion of the nonlife consolidated net operating loss deduction attributable to taxable years subsequent to the year the loss arose), minus such consolidated taxable income recomputed by excluding both that member's items of income and deductions for the absorption year. The deductions of the member include the prior application of this paragraph (m)(3)(vii) to the absorption

of the nonlife consolidated net operating loss deduction for losses arising in taxable years prior to the particular loss year.

(viii) *Election to relinquish carryback.* The offsetable nonlife consolidated net operating loss does not include the amount that could be carried back under paragraph (h) (2) of this section but for the common parent's election under section 172(b)(3)(C) to relinquish the carryback. See section 1503(c)(1).

(ix) *Separate return limitation year.* The offsetable nonlife consolidated net operating and capital loss carryovers do not include any losses attributable to a nonlife member that were sustained (A) in a separate return limitation year (determined without section 1504(b)(2)) of that member (or a predecessor), or (B) in a separate return year ending after December 31, 1980, in which an election was in effect under neither section 1504(c)(2) nor section 243(b)(2). For purposes of this paragraph (m), a separate return limitation year includes a taxable year ending before January 1, 1981. See section 1507(c)(2)(A) of the Tax Reform Act of 1976 and §§1.1502–15 and 1.1502–15A (including applicable exceptions thereto).

(x) *Percentage limitation.* The offsetable nonlife consolidated net operating losses that may be set off against consolidated partial LICTI in a particular year may not exceed a percentage limitation. This limitation is the applicable percentage in section 1503(c)(1) of the lesser of two amounts. The first amount is the sum of the offsetable nonlife consolidated net operating losses under paragraph (m)(2) of this section that may serve in the particular year (determined without this limitation) as a setoff against consolidated partial LICTI. The second amount is consolidated partial LICTI (as defined in paragraph (j) of this section) in the particular year reduced by any nonlife consolidated net capital loss that sets off consolidated partial LICTI in that year.

(xi) *Further limitation.* Any offsetable nonlife consolidated net operating loss remaining after applying the percentage limitation that is carried over to a succeeding taxable year may not be set off against the consolidated partial LICTI attributable to a life member that was not an eligible life member in the year the loss arose. See section 1503(c)(2).

(xii) *Restoration rule.* The carryback of a consolidated LO or life consolidated net capital loss under paragraph (l) of this section that reduces consolidated partial LICTI (or life consolidated capital gain net income) for a prior year may reduce the amount of nonlife subgroup losses that would offset consolidated partial LICTI in that prior year. Thus, that amount may be carried over under paragraph (h) (2) or (4) of this section from that prior year in determining nonlife consolidated taxable income in a succeeding year or serve as offsetable nonlife subgroup losses in a succeeding year.

(4) *Acquired groups.* [Reserved]

(5) *Illustrations.* The following examples illustrates this paragraph (m). In the examples, L indicates a life company, another letter indicates a nonlife company, and each corporation uses the calendar year as its taxable year.

Example (1). P owns all of the stock of L and S. S owns all of the stock of I, a nonlife member that is an ineligible corporation for 1982 under paragraph (d)(13) of this section. For 1982, the group elects under section 1504(c)(2) to file a consolidated return. For 1982, assume that any nonlife consolidated net operating loss may not be carried back to a prior taxable year. Other facts are summarized in the following table.

	Separate taxable income (loss)
P	$100
S	(100)
I	(100)
Nonlife consolidated net operating loss	(100)

Under paragraph (m)(3)(vi) of this section, P's separate income is considered to absorb the loss of S, an eligible member, first and the offsetable nonlife consolidated net operating loss is zero, *i.e.,* the consolidated net operating loss ($100) reduced by I's loss ($100). The consolidated net operating loss ($100) may be carried over, but since it is entirely attributable to I (an ineligible member) its use is subject to the restrictions in paragraph (m)(3)(vi) of this section. The result would be the same if the group contained two additional members, S_1, an eligible member, and I_1, an ineligible member, where S_1 had a loss of ($100) and I_1 had income of $100.

Example (2). The facts are the same as in example (1) except that for 1982 S's separate net operating loss is $200. Assume further that L's consolidated partial LICTI is $200. Under paragraph (m)(3)(vi) of this section, the offsetable nonlife consolidated net operating loss is $100, *i.e.*, the nonlife consolidated net operating loss computed under paragraph (h)(2)(ii) of this section ($200), reduced by the separate net operating loss of I ($100). The offsetable nonlife consolidated net operating loss that may be set off against consolidated partial LICTI in 1982 is $30, *i.e.*, 30 percent of the lesser of the offsetable $100 or consolidated partial LICTI of $200. See paragraph (m)(3)(x) of this section. The nonlife subgroup may carry $170 to 1983 under paragraph (h)(2) of this section against nonlife consolidated taxable income, *i.e.*, consolidated net operating loss ($200) less amount used in 1982 ($30). Under paragraph (m)(2)(ii) of this section, the offsetable nonlife consolidated net operating loss that may be carried to 1983 is $70, *i.e.*, $100 minus $30. The facts and results are summarized in the table below.

	(Dollars omitted)			
	Facts	Offsetable	Limit	Unused loss
	(a)	(b)	(c)	(d)
1. P	100	.....	.....	.....
2. S.	(200)	(100)	.....	(70)
3. I	(100)	.....	.....	(100)
4. Nonlife subgroup	(200)	(100)	(100)	(170)
5. L	200	.....	200	.....
6. 30% of lower of line 4(c) or 5(c)	.....	.....	30	.....
7. Unused offsetable loss	.....	.....	.....	(70)

Accordingly, under paragrah (g) of this section (assuming no amount is withdrawn from L's surplus accounts), consolidated taxable income is $170, *i.e.*, line 5 (a) minus line 6(c)).

Example (3). The facts are the same as in example (2) with the following additions for 1983. The nonlife subgroup has nonlife consolidated taxable income of $50 (all of which is attributable to I) before the nonlife consolidated net operating loss deduction under paragraph (h)(2) of this section. Consolidated partial LICTI is $100. Under paragraph (h)(2) of this section, $50 of the nonlife consolidated net operating loss carryover ($170) is used in 1983 and, under paragraph (m)(3) (vi) and (vii) of this section, the portion used in 1982 is attributable to I, the ineligible nonlife member. Accordingly, the offsetable nonlife consolidated net operating loss from 1982 under paragraph (m)(3)(ii) of this section is $70, *i.e.*, the unused loss from 1982. The offsetable nonlife consolidated net operating loss in 1983 is $24.50, *i.e.*, 35 percent of the lesser of the offsetable loss of $70 or consolidated partial LICTI of $100. Accordingly, under paragraph (g) of this section (assuming no amount is withdrawn from L's surplus accounts), consolidated taxable income is $75.50, *i.e.*, consolidated partial LICTI of $100 minus the offsetable loss of $24.50.

Example (4). P owns all of the stock of S and L. For 1982, all corporations are eligible corporations, and the group elects under section 1504(c)(2) to file a consolidated return, the nonlife consolidated net operating loss is $100, and the nonlife consolidated net capital loss is $50. Assume that the losses may not be carried back and the capital losses are not attributable to built-in deductions under paragraph (m)(3)(ix) of this section or under §1.1502–15A. Other facts and the results are set forth in the following table:

	P–S	L
1. Nonlife consolidated net operating loss	($100)	.....
2. Nonlife consolidated capital loss	(50)	.....
3. Consolidated partial LICTI	.....	$100
4. Life consolidated capital gain net income included in line 3	.....	50
5. Offsetable:		
(a) 30% of lower of line (1) or line (3)–(4)	(15)	.....
(b) Line 2	(50)	.....
(c) Total	(65)	.....
6. Unused losses available to be carried over:		
(a) From line 1 (line 1 minus line 5 (a))	(85)	.....
(b) From line 2 (line 2 minus line 5 (b))	0	.....

Accordingly, under paragraph (g) of this section consolidated taxable income is $35, *i.e.*, line 3 minus line 5(c).

Example (5). The facts are the same as in example (4). Assume further that for 1983 L has an LO that is carried back to 1982 and the LO is large enough to reduce consolidated partial LICTI for 1982 to zero as determined before any setoff for nonlife losses. Under paragraph (m)(3)(xii) of this section, the nonlife consolidated net operating loss of $15 and the nonlife consolidated net capital loss of $50 that were set off in 1982 respectively against consolidated partial LICTI and life consolidated capital gain net income are restored. These restored amounts may consititute part of the nonlife consolidated net operating loss carryover to 1983 under paragraph (h)(2) of this section or part of the

nonlife net capital loss carryover to 1983 under paragraph (h)(4) of this section.

Example (6). The facts are the same as in example (5) except that L's LO for 1983 as carried back reduces consolidated partial LICTI in 1982 from $100 to $25. Since consolidated partial LICTI of $100 in 1982 (before the carryback) included life consolidated capital gain net income of $50, under paragraph (m)(3)(iii) of this section, the life consolidated capital gain net income is $25, *i.e.*, $50 but not more than $25. Therefore, under paragraph (m)(3)(ii) of this section, the offsetable nonlife capital loss in 1982 is $25 and, under paragraph (m) (3)(xii) of this section, $25 of the $50 nonlife consolidated net capital loss in 1982 may be carried under paragraph (h)(4) of this section to 1983. No nonlife consolidated net operating loss is used as a setoff against consolidated partial LICTI in 1982 under paragraph (m)(3)(xii) of this section by reason of the carryback of the consolidated LO from 1983 to 1982.

(n) *Nonlife consolidated taxable income set off by life subgroup losses*—(1) In *general.* The life subgroup losses consist of the consolidated LO and the life consolidated net capital loss (as determined under paragraph (l)(4) of this section). Under paragraph (g)(1) of this section, nonlife consolidated taxable income is set off by the amounts of these two consolidated losses specified in paragraph (n)(2) of this section.

(2) *Amount of setoff.* The portion of the consolidated LO or life consolidated net capital loss that may be set off against nonlife consolidated taxable income (determined under paragraph (h) of this section) is determined by applying the rules prescribed in paragraphs (m) (2) and (3) of this section in the following manner:

(i) Substitute the term ''life'' for ''nonlife'', and vice versa.

(ii) Substitute the term ''nonlife consolidated taxable income'' for ''consolidated partial LICTI'', and vice versa.

(iii) Substitute the term ''consolidated LO'' for ''non-life consolidated net operating loss'', ''paragraph (l)'' or ''paragraph (j)'' for ''paragraph (h)'', and ''section 812(b)(3)'' for ''section 172(b)(3)(C)''.

(iv) Paragraphs (m)(3)(vi), (vii), (x), and (xi) of this section do not apply to a consolidated LO.

(v) Capital losses may not be deducted more than once. See section 818(e) and also the requirements in section 818(f).

(vi) The setoff of life subgroup losses against nonlife consolidated taxable income does not affect nonlife member deductions that depend in whole or in part on taxable income.

(3) *Illustrations.* The following examples illustrate this paragraph (n). In the examples, L indicates a life company, another letter indicates a nonlife company, and each corporation uses the calendar year as its taxable year.

Example (1). P, S, L_1 and L_2 constitute a group that elects under section 1504(c)(2) to file a consolidated return for 1982. In 1982, the nonlife subgroup consolidated taxable income is $100 and there is $20 of nonlife consolidated net capital loss that cannot be carried back under paragraph (h) of this section to taxable years (whether consolidated or separate) preceding 1982. The nonlife subgroup has no carryover from years prior to 1982. Consolidated LO is $150 which under paragraph (l) of this section includes life consolidated capital gain net income of $25. The $150 LO is carried back under paragraph (l)(3) of this section to taxable years (whether consolidated or separate) preceding 1982 before it may offset in 1982 nonlife consolidated taxable income. Since life consolidated capital gain net income is zero for 1982, the nonlife capital loss offset is zero.

Example (2). The facts are the same as in example (1). Assume further that no part of the $150 consolidated LO for 1982 can be used by L_1 and L_2 in years prior to 1982. For 1982, $100 of consolidated LO sets off the $100 nonlife consolidated taxable income. The life subgroup carries under paragraph (l)(3) of this section to 1983 $50 of the consolidated LO ($150 minus $100). See paragraph (l)(3)(ii) of this section. The $50 carryover will be used in 1983 against life subgroup income before it may be used in 1983 to setoff nonlife consolidated taxable income.

Example (3). (a) The facts are the same as in example (1), except that for 1982 the nonlife consolidated taxable income is $150 and includes nonlife consolidated capital gain net income of $50, consolidated partial LICTI is $200, and a life consolidated net capital loss is $50. Assume that the $50 life consolidated net capital loss sets off the $50 nonlife consolidated capital gain net income. Consolidated taxable income under paragraph (g) of this section is $300, *i.e.*, nonlife consolidated taxable income ($150) minus the setoff of the life consolidated net capital loss ($50), plus consolidated partial LICTI ($200).

(b) Assume that for 1983 the nonlife consolidated net operating loss is $150. Under paragraph (h)(2) of this section, the loss may be carried back to 1982 against nonlife consolidated taxable income. If P, the common

parent, does not elect to relinquish the carryback under section 172(b)(3)(C), the entire $150 must be carried back reducing 1982 nonlife consolidated taxable income to zero and nonlife consolidated capital gain net income to zero. Under paragraph (m)(3)(xii) of this section, the setoff in 1982 of the nonlife consolidated capital gain net income ($50) by the life consolidated net capital loss ($50) is restored. Accordingly, the 1982 life consolidated net capital loss may be carried over by the life subgroup to 1983. Under paragraph (g) of this section, after the carryback consolidated taxable income for 1982 is $200, *i.e.*, nonlife consolidated taxable income ($0) plus consolidated partial LICTI ($200).

Example (4). The facts are the same as in example (3), except that P elects under section 172 (b)(3)(C) to relinquish the carryback of $150 arising in 1983. The setoff in part (a) of example (3) is not restored. However, the offsetable nonlife consolidated net operating loss for 1983 (or that may be carried forward from 1983) is zero. See paragraph (m)(3)(viii) of this section. Nevertheless, the $150 nonlife consolidated net operating loss may be carried forward to be used by the nonlife group.

Example (5). P owns all of the stock of S_1 and of L_1. On January 1, 1978, L_1 purchases all of the stock of L_2. For 1982, the group elects under section 1504(c)(2) to file a consolidated return. For 1982, L_1 is an eligible corporation under paragraph (d)(12) of this section but L_2 is ineligible. Thus, L_1 but not L_2 is a member for 1982. For 1982, L_2 sustains an LO that cannot be carried back. For 1982, L_2 is treated under paragraph (f)(6) of this section as a member of a controlled group of corporations under section 1563 with P, S, and L_1. For 1983, L_2 is eligible and is included on the group's consolidated return. L_2's LO for 1982 that may be carried to 1983 is not treated under paragraph (d)(11) of this section as having been sustained in a separate return limitation year for purposes of computing consolidated partial LICTI of the L_1–L_2 life subgroup for 1983. Furthermore, the portion of L_2's LO not used under paragraph (l)(3) of this section against life subgroup income in 1983 may be included in offsetable consolidated operations loss under paragraph (n)(2) and (m)(3)(i) of this section that reduces in 1983 nonlife consolidated taxable income because L_2's loss in 1982 was not sustained in a separate return limitation year under paragraph (n)(2) and (m)(3)(ix)(A) of this section or in a separate return year (1982) when an election was in effect neither under section 1504(c)(2) nor section 243(b)(2).

(o) *Alternative tax*—(1) *In general.* For purposes of the alternative tax under paragraph (f)(7)(ii) of this section, consolidated net capital gain is the sum of the following two amounts:

(i) The nonlife consolidated net capital gain reduced by any setoff of a life consolidated net capital loss.

(ii) The life consolidated net capital gain reduced by any setoff of a nonlife consolidated net capital loss.

(2) *Net capital gain.* For purposes of this paragraph (o):

(i) Nonlife consolidated net capital gain is computed under §§1.1502–41A or 1.1502–22T (as appropriate) except that it may not exceed nonlife consolidated taxable income (computed under paragraph (h) of this section).

(ii) Life consolidated net capital gain is computed under §§1.1502–41A or 1.1502–22T (as appropriate), applied in a manner consistent with paragraph (l)(4) of this section, except that it may not exceed consolidated partial LICTI (as determined under paragraph (j) of this section).

(iii) *Setoffs.* Setoffs are determined under paragraphs (m) or (n) of this section (as the case may be).

(p) *Transitional rule for credit carryovers.* For limitations on credits arising in taxable years ending before January 1, 1981, that may be carried over to taxable years beginning on or after that date, section 1507(c)(2)(A) of the Tax Reform Act of 1976 and the principles in paragraph (h)(3) of this section (relating to limitations on loss carryovers) apply.

(q) *Preemption.* The rules in this section preempt any inconsistent rules in other sections (§1.1502–1 through 1.1502–80) of the consolidated return regulations. For example, the rules in paragraph (m)(3)(vi) apply notwithstanding §§1.1502–21A(b)(3) and 1.1502–79A(a)(3) (or §1.1502–21, as appropriate).

(r) *Other consolidation principles.* The fact that this section treats the life and nonlife members as separate groups in computing, respectively, consolidated partial LICTI (or LO) and nonlife consolidated taxable income (or loss) does not affect the usual rules in §§1.1502–0—1.1502–80 unless this section provides otherwise. Thus, the usual rules in §1.1502–13 (relating to intercompany transactions) apply to both the life and nonlife members by treating them as members of one affiliated group.

(s) *Filing requirements.* Nonlife consolidated taxable income or loss under

paragraph (h) of this section shall be determined on a separate Form 1120 or 1120 M and consolidated partial LICTI under paragraph (j) of this section shall be determined on a separate Form 1120 L. The consolidated return shall be made on a separate Form 1120, 1120 M, or 1120 L by the common parent (if the group includes a life company), which shows the set-offs under paragraphs (g), (m), and (n) of this section and clearly indicates by notation on the face of the return that it is a life-nonlife consolidated return (if the group includes a life company). See also §1.1502–75(j), relating to statements and schedules for subsidiaries.

(Secs. 1502 and 7805 of the Internal Revenue Code of 1954 (68A Stat. 637, 917; 26 U.S.C. 1502, 7805))

[T.D. 7877, 48 FR 11441, Mar. 18, 1983, as amended by T.D. 7912, 48 FR 40215, Sept. 6, 1983; T.D. 8560, 59 FR 41674, Aug. 15, 1994; T.D. 8597, 60 FR 36679–36680, July 18, 1995; T.D. 8677, 61 FR 33324, June 27, 1996; T.D. 8823, 64 FR 36100, July 2, 1999]

§1.1502–55 Computation of alternative minimum tax of consolidated groups.

(a) through (h)(3) [Reserved]

(h)(4) *Separate return year minimum tax credit.*

(i) and (ii) [Reserved]

(iii)(A) *Limitation on portion of separate return year minimum tax credit arising in separate return limitation years.* The aggregate of a member's minimum tax credits arising in SRLYs that are included in the consolidated minimum tax credits for all consolidated return years of the group may not exceed—

(*1*) The aggregate for all consolidated return years of the member's contributions to the consolidated section 53(c) limitation for each consolidated return year; reduced by

(*2*) The aggregate of the member's minimum tax credits arising and absorbed in all consolidated return years (whether or not absorbed by the member).

(B) *Computational rules—*(*1*) *Member's contribution to the consolidated section 53(c) limitation.* Except as provided in the special rule of paragraph (h)(4)(iii)(B)(*2*) of this section, a member's contribution to the consolidated section 53(c) limitation for a consolidated return year equals the member's share of the consolidated net regular tax liability minus its share of consolidated tentative minimum tax. The group computes the member's shares by applying to the respective consolidated amounts the principles of section 1552 and the percentage method under §1.1502–33(d)(3), assuming a 100% allocation of any decreased tax liability. The group makes proper adjustments so that taxes and credits not taken into account in computing the limitation under section 53(c) are not taken into account in computing the member's share of the consolidated net regular tax, etc. (See, for example, the taxes described in section 26(b) that are disregarded in computing regular tax liability.)

(*2*) *Adjustment for year in which alternative minimum tax is paid.* For a consolidated return year for which consolidated tentative minimum tax is greater than consolidated regular tax liability, the group reduces the member's share of the consolidated tentative minimum tax by the member's share of the consolidated alternative minimum tax for the year. The group determines the member's share of consolidated alternative minimum tax for a year using the same method it uses to determine the member's share of the consolidated minimum tax credits for the year.

(*3*) *Years included in computation.* For purposes of computing the limitation under this paragraph (h)(4)(iii), the consolidated return years of the group include only those years, including the year to which a credit is carried, that the member has been continuously included in the group's consolidated return, but exclude any years after the year to which the credit is carried.

(*4*) *Subgroup principles.* The SRLY subgroup principles under §1.1502–21(c)(2) apply for purposes of this paragraph (h)(4)(iii). The predecessor and successor principles under §1.1502–21(f) also apply for purposes of this paragraph (h)(4)(iii).

(*5*) *Overlap with section 383.* The principles under §1.1502–21(g) apply for purposes of this paragraph (h)(4)(iii). For example, an overlap of this paragraph (h)(4)(iii) and the application of section 383 with respect to a credit carryover